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Maekawa Commission Report Unveiled

A panel of advisers to Prime Minister Yasuhiro Nakasone formally submitted a report April 7 calling for changes in Japan's export-oriented industrial structure to reduce the nation's current account surplus. The Advisory Group on Economic Structural Adjustment for International Harmony, headed by former Bank of Japan governor Haruo Maekawa, produced an 11-page report following five months of debate.

The report outlines principles for transforming Japan's economy to growth based on domestic demand (see JEI Report No. 13B, April 4, 1986). To

Although England and West Germany have completed arrangements to allow SDI participation, Tokyo has remained cautious toward the program for a variety of political and technical reasons. Nevertheless, the Department of Defense's emphasis on Japanese involvement remains high due to Japan's unquestioned status as a potentially significant contributor to the research. Pentagon officials are also interested in Japanese cooperation in light of Tokyo's cap of 1 percent of gross domestic product on overall defense spending. While it is unlikely that the program would founder without Japanese participation, it appears that DOD feels the plan's chances for success would be much greater with it. Although the nature of Japanese participation is uncertain, most observers feel that Tokyo will be involved in the program. A decision is expected by the May summit at the latest.

Mr. Weinberger also used the Japan leg of his Far Eastern tour to focus attention on other security issues by beginning his visit in Hokkaido. The secretary's presence on the island drew attention to Japan's dispute with the Soviet Union over the status of four islands just to its north. Both countries' claim to the islands presents a serious obstacle to improved relations and the negotiation of a peace treaty. Mr. Weinberger's stopover helped underscore American support for the Japanese position in the dispute. In addition, Mr. Weinberger observed units of the Ground Self-Defense Forces, thereby implicitly emphasizing their importance in the defense of Japan. The GSDF have come under severe pressure in recent years, as budget and security analysts have called for increased utilization of Air and Maritime Self-Defense Forces while reducing the land element to provide more effective -- and less costly -- defense. In effect, the secretary of defense underscored the continued need for the GSDF without injecting himself into the discussion of Japan's most appropriate defense role and force level.

Michael W. Chinworth

Trade Gap Continues To Separate China And Japan

Trade continues to dominate Japan's relations with China despite economic reforms by both countries aimed at alleviating trade pressures. While Japan chalked up a record trade surplus in 1985 with its giant communist neighbor, the two nations recently signed a five-year pact that will promote even greater trade flows. Chinese leaders have hinted that a political solution to the trade imbalance must be reached, a suggestion that Tokyo has staunchly resisted.

At the heart of the problem lies the phenomenal growth of the bilateral trade imbalance. Japan's exports to China surpassed its imports in 1984 for the first time, but the difference was relatively minor at $1.3 billion. In 1985, however, Japanese exports grew 72.9 percent while imports rose only 8.8 percent, pushing the surplus up to just under $6 billion (see Table). Movements of this magnitude have understandably caught the attention of Beijing.

Throughout the second half of 1985, Chinese leaders maintained a chorus of warnings that the rapidly deteriorating bilateral trade situation was unacceptable and that if Japan did not act to slow its exports, Beijing would. The Japanese responded that the sharp rise in trade was due to the far-reaching

Japan's Trade With China, 1984-85

(in millions of dollars)

	1984	1985
Exports		
Food	$20.5	$19.9
Textiles and Apparel	382.6	471.4
Synthetic Yarn	70.6	107.9
Clothing	3.9	4.8
Chemicals	610.2	713.0
Fertilizers	16.5	12.1
Pharmaceuticals	14.8	14.7
Plastics	254.8	349.2
Nonmetallic Mineral Manufactures	47.0	90.5
Metals and Fabricated Metal Products	2,842.8	3,529.9
Steel	2,668.1	3,192.6
Nonferrous Metals	80.3	164.5
Metal Products	94.5	172.8
Nonelectric and Electric Machinery	2,961.4	7,106.1
Nonelectric Power Generating Equipment	70.9	112.0
Office Machinery	67.8	122.7
Metalworking Equipment	47.7	182.7
Textile Equipment	83.3	271.9
Electric Power Machinery	40.1	112.6
Televisions	363.9	1,073.6
Radios	49.2	94.0
Electronic Components	70.7	160.3
Motor Vehicles	471.2	1,501.6
Motorcycles	68.9	205.1
Precision Equipment	142.4	250.3
Other	352.1	546.6
Total	7,216.7	12,477.4
Imports		
Food	630.3	934.7
Textile Raw Materials	286.4	354.7
Metal Ores and Scrap	9.7	9.3
Other Raw Materials	503.9	463.0
Soybeans	103.9	75.9
Mineral Fuels	3,093.1	2,970.0
Coal	204.3	184.0
Crude Oil	2,314.8	2,198.8
Petroleum Products	542.7	586.1
Chemicals	247.8	301.9
Pharmaceuticals	17.7	17.6
Nonelectric and Electric Machinery	14.7	18.1
Metalworking Equipment	1.0	1.7
Precision Equipment	5.4	7.0
Other	1,171.9	1,430.9
Steel	7.7	4.3
Nonferrous Metals	32.3	84.8
Textiles	888.0	956.8
Toys and Games	1.9	3.0
Total	5,957.6	6,482.7

Source: Japan Tariff Association, The Summary Report: Trade of Japan

economic reform programs that Beijing was implementing. The increased use of free-market mechanisms and decentralized economic planning, particularly for investment decisions, played havoc with China's foreign exchange reserves and trade flows. Several cases of improper activities were uncovered in China's special economic zones (areas that enjoy significant economic autonomy and are meant to be showcases for development), which added to the pressure on Beijing to reassert economic control. Japan's hands were not exactly spotless either, however. In one well-publicized case, used cars and motorcycles were sold as new, and in another, faulty refrigerators and air conditioners were delivered. Despite these unsavory instances, Chinese consumers avidly purchased Japanese electronic and household appliances whenever possible. Decades of frugality clearly resulted in a great amount of pent-up demand.

By late 1985, in an effort to slow the accumulation of red ink, China had clamped down on foreign exchange transactions, new and existing contracts, and the importation of several items, including cars and other consumer durables. Although this led to some grumbling by Japan's smaller trading companies, Tokyo acknowledged the need for action. In mid-January, Japan committed itself to buying more coal, crude oil, petroleum products and agricultural commodities from China over the next five years. The agreement will mean purchases of 8.8-9.3 million metric tons of crude oil a year (up from just under 8 million metric tons in 1985) and 3.7-4.1 million metric tons of coal. Discussions on purchases of agricultural products and light manufactures, particularly textiles, will be held within the year.

For its part, China has reiterated its commitment to its ambitious growth plans, signaling its intent to remain open to foreign trade. At the same time, however, Chinese leaders have also called for swift, cooperative action if the trade imbalance remains at present levels. Beijing does not enjoy being in debt to anyone and, unlike Tokyo, it can institute draconian measures if the need arises. Both countries are therefore expected to work out guidelines for a more stable economic relationship, which will probably entail greater direct investment and technology transfers from Japan to China.

Jon Choy

Europeans Try New Tack On Trade Relations With Japan

The European Community is apparently changing course in its efforts to find a solution to its growing trade deficit with Japan. After years of pressing Tokyo to tear down a broad range of tariff and nontariff trade barriers, the EC leadership is now pressing for negotiations on specific products. The inspiration for this approach clearly comes from the just completed U.S.-Japan market-oriented, sector-selective (MOSS) talks. In addition, however, the EC has suggested that it may question Japan's trade privileges resulting from adherence to the General Agreement on Tariffs and Trade. Such a suspension of GATT treatment would be unprecedented, and it is unclear exactly how it might be done.

EC foreign ministers adopted the surprisingly harsh stance on March 10 at a meeting dealing specifically with Japan. Despite an Executive Commission recommendation for a less confrontational policy, the Executive Council made